

Squeeze-out Mechanisms Applicable to Non-listed Companies

BY PAWEŁ SIKORA | KUBAS KOS GAERTNER

Not only are listed companies exposed to takeovers, control change may occur in non-listed companies as well, although for obvious reasons the latter are less vulnerable to unsolicited takeover. An important puzzle of the entire legal framework facilitating takeovers is the squeeze-out mechanism. Squeeze-out is understood as a means of compulsory acquisition of the residual shares of the target. In many jurisdictions squeeze-out only exists for listed companies. This is not the case in Poland, where there is a separate set of rules applicable to non-listed companies. This article discusses practical problems associated with the compulsory acquisition of non-listed companies under Polish law.

Private equity firms may take advantage of the squeeze-out mechanism regulated by the law (Article 418 of the Code of Commercial Companies). However, the Code introduces certain conditions, the fulfilment of which such a possibility shall depend on. And so effecting a squeeze-out shall be possible only in joint-stock companies in which no more than five shareholders jointly hold not less than 95% of the entire share capital and at the same time each of these shareholders holds not less than 5% of the share capital. The squeeze-out takes place on the grounds of a resolution of the general shareholder meeting and to become effective requires a qualified majority of 95% of the votes (whereas the articles of association may introduce stricter requirements). In order to foster shareholder democracy with respect to such a fundamental decision, which many want to perceive as a private expropriation, the law mandatorily introduces the one share-one vote principle. The resolution should specify the stocks subject to the squeeze-out as well as identify the shareholders who adopt the obligation to redeem the shares. It is proper to point out that the act does not require the resolution on the squeeze-out to contain any substantiation by the company's bodies whatsoever.

A relevant element intended to constitute the securing of the minority stockholders' interests is the duty for the price to be established by an expert appointed by the shareholder meeting (or in the case the shareholder meeting fails to do so – by the registry court). *The squeeze-out price is announced at the shareholder meeting.* What is of relevance – the company has the obligation to submit the expert's valuation to the registry court while shareholders questioning the price amount, on the basis of the motion filed with the court, may demand verification of the price set. In any case, the company itself is entitled to the same right. The court's decision on this subject is final and the squeeze-out price set by the court shall not be subject to any changes. Therefore, it must be noted that insofar as the minority shareholders are unable to oppose their exclusion from the corporation, then the act guarantees them the possibility of verifying the price which their shares shall be purchased for.

What is clear, the shareholders whose shares are subject to a squeeze-out are not deprived of the protection provided by the possibility of challenging the resolution of the shareholder meeting. Also in this case, a possibility of demanding the ascertainment of the invalidity of the resolution exists in the event it was adopted with the breach of the law or, relatively, to demand that the resolution is reversed in case it stands in contradiction with the articles of association or good practice and in case it aimed against the company's interest or when it is intended to cause detriment to a shareholder. Insofar as the ascertainment of the invalidity on the grounds of the violation of mandatory provisions of the law does not stir any doubts, then it is worth taking a look at the other of the possibilities, and in particular at the premise of causing detriment to a shareholder and being aimed against

the company's interests. However, it is proper to point out that taking advantage of the squeeze-out institution by majority stockholders *shall not constitute the reason for the reversal of the resolution* if it is based on the recourse to the provisions of the law in force. Such a view is well-established in Polish law as the compliance of the squeeze-out with the Constitution of the Republic of Poland was pronounced by the Constitutional Tribunal in 2004. For this reason it is indispensable to demonstrate certain additional circumstances which shall decide upon the detriment to a given shareholder (it may so happen that in the case of the existence of additional agreements – e.g., a call option on the shares – providing the grounds for the change of the shareholding status by such a small shareholder, and the ordering of a squeeze-out would render the realisation of such rights impossible).

At the moment of the payment of the entire squeeze-out price by the redeeming stockholders and the carrying out of the squeeze-out by the company's management board (on behalf of the stockholders), minority shareholders lose their titles. Therefore, this is yet another defensive mechanism. If the redeeming stockholders want to exercise the rights from the newly acquired stocks, they must pay the squeeze-out price beforehand. The squeeze-out price is paid to the company while the former stockholders entertain a claim for the payment of an appropriate amount towards the company. It is proper to note here that the provisions of the act contain no detailed regulation in the scope of the transfer of the squeeze-out price onto stockholders. Therefore, the company has no special rights in relation to its creditors which means that also at this stage the former stockholders may hinder the completion of the procedure by evading the acceptance of the performance. Although such actions shall be devoid of significance for the effectiveness of the procedure performed, it may constitute quite a complication for the company (in particular in case the number of the squeezed out shareholders is significant).

Another, though more costly and risky operation aiming at the exclusion of residual shareholders that the majority may attempt to avail itself of is the application of the so-called *freeze out* which consists in the establishment of a new company and then the adoption by the company which the minority stockholders are to be eliminated from, of a resolution on the sale of this company's enterprise to the benefit of the newly established company. The requirement for the adoption of such a resolution is the a three-quarters majority vote. In the exercise of the adopted resolution, the company sells its organised assets (in total or in the respective part) and next, a resolution on the liquidation of the company is adopted whereby – as a result of the division of the estate – all shareholders receive the value of the stocks they hold. Therefore, it is proper to note that the operation thus conducted realises the function of the squeeze-out institution. The operations conducted so far by the liquidated company have been taken over by the company in which stockholders are *exclusively entities being the majority shareholders of the liquidated company*. Therefore, the issue here is not only the "squeeze-out" of the minority shareholders from the company since it ceases to exist, and only providing the majority shareholders with the exclusive control over the company's organised assets within the frames of a new entity (as a passive investor). In relation to the squeeze-out, this solution has the disadvantage that it is a much more complicated process requiring that majority stockholders incur substantial outlays with the view of guaranteeing the new company the financing for the purchase of the organised assets. It is also proper to note that minority shareholders hold no specific rights enabling them to oppose the disposal of the enterprise and then the liquidation of the company whatsoever, since this process may be conducted without the breach of the provisions of the law providing the basis for the ascertainment of its invalidity. In principle there is no basis to demand the reversal of this resolution as aimed against the interests of the minority shareholders since the company is dissolved and all the shareholders

receive the value of the stocks they hold. However, one may not rule out the possibility that the court allows the charge of abuse of the substantive right by a majority stockholder.

Pawel Sikora is an Associate at Kubas Kos Gaertner.



[Click here to view COMPANY profile](#)